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IN THE

Supreme Court of the United States

OCTOBER TERM, 1950.

No. 686

FEDERAL LIQUIDATING CORPORATION,
PETITIONER,

v.

SECURITIES AND EXCHANGE COMMISSION

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT.

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FEDERAL LIQUIDATING CORPORATION, PETITIONER,

v.

SECURITIES AND EXCHANGE COMMISSION.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT.

Federal Liquidating Corporation prays that a writ of certiorari issue to review a final judgment of the United States Court of Appeals for the Second Circuit, entered in the above-entitled case on April 9, 1951, affirming a Supplemental Order of the Securities and Exchange Commission, dated June 19, 1950.

Opinions Below.

The Commission's Findings, Opinion and Order dated September 11, 1947 (R. 35), and its Supplemental Order dated June 19, 1950 (R. 196), together with its Supplemental Findings and Opinion dated July 28, 1950 (R. 199), have not yet been officially reported but are set forth in the Commission's Holding Company Act Release Numbers 7701 and 9981. The opinion of the court below (R. 262) has not yet been reported.

Jurisdiction.

The judgment of the Court of Appeals for the Second Circuit was entered on April 9, 1951 (R. 272). No petition for rehearing has been filed. The jurisdiction of this Court is invoked under 1948 Revised Judicial Code, c. 646, 62 Stat. 928 (28 U. S. C. §1254), made applicable by Section 25 of the Public Utility Holding Company Act of 1935, 49 Stat. 803 (15 U. S. C. §79, *et seq.*). This petition is being filed in conformity with, and within the time limited by the provisions of Rule 38 of the Rules of this Court and U. S. C., Title 28, Section 2101(c) (62 Stat. 961, 63 Stat. 104).

Questions Presented.

In accordance with a Section 11(e) Plan approved by the Commission, Federal Light & Traction Company, a public utility holding company, was dissolved by the favorable vote of the holders of at least two-thirds of its outstanding capital stock as required by and pursuant to the provisions of the New York statute governing *voluntary* dissolution.[1] This gives rise to important questions of federal law not previously decided by this Court. Under the provisions of the charter, the preferred stock was entitled to $100 per share upon liquidation, whether *voluntary* or involuntary, and to $110 per share upon call or redemption, together in each case with accrued dividends. The following questions are presented:

1. Did the Commission properly apply the "fair and equitable" standard of Section 11(e) of the Public Utility Holding Company Act in finding that the preferred stockholders were entitled to receive an amount equal to the call

[1] New York Stock Corporation Law, §105.

price of their shares, where this amount exceeds the *voluntary* charter liquidation preference of such shares?

2. Did the Commission properly apply the "fair and equitable" standard of Section 11(e) in awarding to the preferred stockholders more than the amount of the *voluntary* charter liquidation preference, where a holding company, after divesting itself of properties not retainable under the integration standards of Section 11(b)(1), could have continued its existence as such for operating public utility subsidiaries permitted to be retained by it under the integration standards, and it voluntarily causes itself to be liquidated and dissolved by appropriate action of its stockholders?

3. Where a holding company had disposed of properties representing more than 50% of its total investment prior to the issuance of the Commission's first divestment order, and the Commission has conceded in its findings that strong business reasons for making such dispositions existed apart from the integration requirements of the Act, did the Commission properly determine the fair investment value of the preferred stock on a basis which gave no weight whatsoever to the possibility of liquidation of the holding company for reasons existing apart from the requirements of the Act?

4. Did the Commission properly determine the fair investment value of the preferred stock, where such determination is based in part upon the inclusion of earnings of, and dividends from, subsidiaries which had been disposed of prior to the time that liquidation took place, and in part upon the assumed investment of excess cash in common stocks of hypothetical operating companies?

5. Where, as part of a Section 11(e) plan, the Commission has approved the issuance to the preferred stockholders of Certificates of Contingent Interest in an escrow fund, and has approved the amount of the fund and the terms and conditions of the Certificates, did the Commission properly determine that the holders of the Certificates are entitled to an aggregate payment in excess of the aggregate amount available in the fund and payable under the terms and conditions of the Certificates?[2]

Statute Involved.

Section 11(e) of the Public Utility Holding Company Act of 1935, provides as follows:

> "(e) In accordance with such rules and regulations or order as the Commission may deem necessary or appropriate in the public interest or for the protection of investors or consumers, any registered holding company or any subsidiary company of a registered holding company may, at any time after January 1, 1936, submit a plan to the Commission for the divestment of control, securities, or other assets, or for other action by such company or any subsidiary company thereof for the purpose of enabling such company or any subsidiary company thereof to comply with the provisions of subsection (b). If, after notice and opportunity for hearing, the Commission shall find such plan, as submitted or as modified, necessary to effectuate the provisions of subsection (b) and fair and equitable to the persons affected by such plan, the Commission shall make an order approving such plan; and the Commission, at the request of the company, may apply

[2] Although the court below is divided on this issue, the amount involved is small, and, accordingly, we do not seek review unless it is granted on the basis of one of the more general and important questions above set forth.

to a court, in accordance with the provisions of subsection (f) of section 18, to enforce and carry out the terms and provisions of such plan. If, upon any such application, the court, after notice and opportunity for hearing, shall approve such plan as fair and equitable and as appropriate to effectuate the provisions of section 11, the court as a court of equity may, to such extent as it deems necessary for the purpose of carrying out the terms and provisions of such plan, take exclusive jurisdiction and possession of the company or companies and the assets thereof, wherever located; and the court shall have jurisdiction to appoint a trustee, and the court may constitute and appoint the Commission as sole trustee, to hold or administer, under the direction of the court and in accordance with the plan theretofore approved by the court and the Commission, the assets so possessed."

Section 24 (a) of the same act, provides as follows:

"(a) Any person or party aggrieved by an order issued by the Commission under this title may obtain a review of such order in the circuit court of appeals of the United States within any circuit wherein such person resides or has his principal place of business, or in the United States Court of Appeals for the District of Columbia, by filing in such court, within sixty days after the entry of such order, a written petition praying that the order of the Commission be modified or set aside in whole or in part. A copy of such petition shall be forthwith served upon any member of the Commission, or upon any officer thereof designated by the Commission for that purpose, and thereupon the Commission shall certify and file in the court a transcript of the record upon which the order complained of was entered. Upon the filing of such transcript such court shall have exclusive jurisdiction to affirm, modify, or set aside such order, in whole or in part.

No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission or unless there were reasonable grounds for failure so to do. The findings of the Commission as to the facts, if supported by substantial evidence, shall be conclusive. If application is made to the court for leave to adduce additional evidence and it is shown to the satisfaction of the court that such additional evidence is material and that there were reasonable grounds for failure to adduce such evidence in the proceeding before the Commission, the court may order such additional evidence to be taken before the Commission and to be adduced upon the hearing in such manner and upon such terms and conditions as to the court may seem proper. The Commission may modify its findings as to the facts by reason of the additional evidence so taken, and it shall file with the court such modified or new findings, which, if supported by substantial evidence, shall be conclusive, and its recommendation, if any, for the modification or setting aside of the original order. The judgment and decree of the court affirming, modifying, or setting aside, in whole or in part, any such order of the Commission shall be final, subject to review by the Supreme Court of the United States upon certiorari or certification as provided in sections 239 and 240 of the Judicial Code, as amended (U. S. C., title 28, secs. 346 and 347)."

Statement.

This case involves a plan (the "Plan") filed under Section 11(e) of the Public Utility Holding Company Act of 1935 (the "Act") by Federal Light & Traction Company ("Federal"), Cities Service Company ("Cities"), Public Service Company of New Mexico ("Public Service"), and Federal Liquidating Corporation ("Liquidating

Corporation"). At the time of the Commission's Findings, Opinion and Order, dated September 11, 1947, approving the Plan, Federal was a subsidiary of Cities and both were registered holding companies, Public Service was an operating utility subsidiary of Federal, and Liquidating Corporation (the petitioner) was a newly formed corporation which had been organized for the purpose of facilitating the liquidation of Federal in accordance with the Plan. The original application was filed in September, 1946, and hearings on the Plan were held in November, 1946.

The Commission's Order of September 11, 1947, approving the Plan, reserved jurisdiction with respect to the additional amount, if any, which the preferred stockholders of Federal are entitled to receive in excess of $100 per share plus accrued and unpaid dividends to the date of dissolution of Federal, being the amount which they are entitled to receive under the provisions of Federal's charter upon liquidation, dissolution or winding up, whether voluntary or involuntary. Federal, a New York corporation, was voluntarily dissolved in accordance with New York law pursuant to authorization voted at a special meeting of stockholders held on October 2, 1947. Federal was liquidated on or about October 15, 1947.

In accordance with the Plan (a) there was distributed to Federal's preferred stockholders upon the surrender of their stock certificates $100 per share in cash plus accrued and unpaid dividends and Certificates of Contingent Interest in the Escrow Fund described in (c) below; (b) there was distributed to Federal's common stockholders upon the surrender of their stock certificates $11 per share in cash and common stock on a share for share basis of Public Service and of Liquidating Corporation; (c) Federal deposited with The New York Trust Company, as escrow agent, under an Escrow Agreement (the "Escrow Agree-

ment") between Federal, Liquidating Corporation and The New York Trust Company, the sum of $496,923.24 (the "Escrow Fund"), which is equivalent to the aggregate premium of $10 per share to which the preferred stock would be entitled upon redemption ($426,910), plus $70,013.24, which represents interest for approximately three years on the maximum amount of premium computed at 5.45%, the yield of a $6 preferred stock based on a redemption price of $110; and (d) Federal transferred all of its remaining assets, consisting principally of cash, to Liquidating Corporation, which assumed all of Federal's liabilities.

Under the terms of the Escrow Agreement, any moneys in the Escrow Fund not required to be paid to the holders of the Certificates of Contingent Interest (preferred stockholders) will be paid over to Liquidating Corporation.

Hearings on the reserved issue were begun before the Trial Examiner on October 29, 1947, were resumed on December 15 and concluded on December 16, 1947. At these hearings financial and other data concerning Federal and its subsidiaries was introduced in evidence, including evidence that Federal had been dissolved and liquidated by action of its stockholders in full compliance with the applicable New York statutes (R. 66-74). In addition, there was testimony by an officer of Federal who had participated intimately in its affairs for many years. This witness described the circumstances surrounding the various property dispositions and testified that, apart from the impact of Section 11 of the Act, Federal would have been liquidated shortly following January 1, 1946, the date on which the repeal of the excess profits tax law became effective (R. 106). The record shows that, of the 25 companies which had comprised the system when the Act went into effect in 1935 (R. 203), almost half of that number, representing

more than 50% of Federal's total investment, had been disposed of prior to the issuance on August 17, 1943 of the Commission's first divestment order[3] in Section 11(b)(1) integration proceedings. In its Supplemental Findings and Opinion, the Commission conceded that strong business reasons existed for these divestments aside from the necessity of complying with the Act (R. 210). The record also shows that of the remaining subsidiaries, only five of any consequence were actually ordered to be divested and that only one of these was of substantial importance in the system (R. 210-214). Under the Commission's integration orders[4], Federal was permitted to retain four subsidiaries operating in New Mexico and one in Colorado.

Briefs were filed and oral argument was held before the Commission on March 23, 1950. On June 19, 1950, the Commission issued its Supplemental Order (R. 196-198) in which it ordered that the holders of the Certificates of Contingent Interest be paid the amount of $10 for each share of preferred stock represented by said Certificates, together with compensation for the delay in payment of said amounts at the rate of 5.45% per annum from October 2, 1947, to the date of payment, and on July 28, 1950 the Commission issued its Supplemental Findings and Opinion (R. 199-245) in support of said Supplemental Order.

The Commission rejected Federal's contention that the voluntary charter liquidation preference should be solely controlling in determining the rights of the stockholders upon liquidation, on the ground that the liquidation and dissolution of Federal was effected to comply with the

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[3] *Cities Service Power & Light Company*, H. C. A. Release No. 4489 (1943).

[4] *Cities Service Power & Light Company*, H. C. A. Release No. 4489 (1943); *Federal Light & Traction Company*, H. C. A. Release No. 4960 (1944).

requirements of the Act (R. 206-207). The Commission also rejected Federal's contention that the probability of liquidation of Federal, apart from the Act, was so great as to render the voluntary charter liquidation preference solely controlling, holding that absent the impact of the Act "liquidation for purely business reasons would not have occurred, and that, therefore, the liquidation preference ceases to be a dispositive factor in determining the investment value of the preferred stock." (R. 219).

On August 18, 1950, Liquidating Corporation petitioned the United States Court of Appeals for the Second Circuit for review (R. 1A) of the Commission's Supplemental Order of June 19, 1950. Briefs were filed and oral argument heard by the Court of Appeals on February 6-7, 1951. On March 16, 1951, the Court of Appeals issued its Opinion affirming the Order of the Commission (R. 262).

The Court of Appeals held that the voluntary charter liquidation preference could not be regarded as solely controlling in view of the decisions of this Court in *Otis & Co.* v. *Securities & Exchange Commission*, 323 U. S. 624, and *Securities and Exchange Commission* v. *Central-Illinois Securities Corp.*, 338 U. S. 96. The Court below also upheld the Commission's determination that liquidation of Federal would not have occurred apart from the impact of the Act, and it refused to disturb the method by which the Commission determined the fair investment value of the preferred stock (R. 267-270). The Court, with one judge dissenting, rejected Liquidating Corporation's contention that the payment to the holders of Certificates of Contingent Interest should, in any event, be limited to the amount in the Escrow Fund (R. 270-271).

Reasons for Granting the Writ.

This case involves issues of substantial importance in the administration of the Public Utility Holding Company Act not previously decided by this Court. This Court has had occasion to consider the "fair and equitable" standard of Section 11(e) of the Act in two cases, namely, *Otis & Co.* v. *Securities & Exchange Commission*, 323 U. S. 624 (1945) and *Securities and Exchange Commission* v. *Central-Illinois Securities Corp.*, 338 U. S. 96 (1949). In both of those cases, however, the principal question before the Court was whether the *involuntary* charter liquidation preference is the sole measure in determining the equitable equivalent of the securities surrendered where liquidation of a holding company is compelled by the Act. In such a context this Court held that the *involuntary* charter liquidation preference does not of itself determine the amounts shareholders are to receive upon a liquidation compelled by the requirements of the Act, for the reason that the legislative policy embodied in the Act "was not foreseeable." (323 U. S. at p. 638 and 338 U. S. at p. 132). The issue in the instant case is substantially different from that in the *Otis* and *Central-Illinois* cases, since it involves the effect to be given to the *voluntary* charter liquidation preference where liquidation actually has been or demonstrably can be consummated by the voluntary action of the holding company and its stockholders in accordance with state law. It is believed that the determination of this issue under the circumstances of this case will have an important bearing in other cases now in litigation or pending before the Commission, and that the same is true with respect to issues in this case relating to the determination of the fair invest-

ment value of the preferred stock. It is further believed that an important question is presented with regard to the scope of the findings required to be made by an administrative agency in support of its decision.

I.

1. Both the Commission and the Court of Appeals have treated this case as falling within the purview of the *Otis* and *Central-Illinois* cases. They have so held on the basis of the Commission's finding that the ultimate decision to liquidate Federal was the result of the actual or potential impact of the integration requirements of the Act (R. 219, 268), and that in such circumstances the *voluntary* charter liquidation preference is not determinative of the rights of the shareholders, despite the fact that the liquidation and dissolution of Federal was proposed to be and actually was consummated by the voluntary action and the required vote of its stockholders in accordance with the applicable provisions of New York law (R. 202).

In the *Otis* case, United Light & Power Co., which had been ordered by the Commission to dissolve, filed a plan in which it undertook to satisfy its creditors and to distribute its remaining assets to its preferred and common stockholders. The plan was to be consummated by exercise of the powers conferred upon the Commission and the courts by the latter portion of Section 11(e). The plan was not proposed to be, nor could it have been, consummated by stockholder action. Because of the large arrears of dividends on the preferred stock, the holders thereof would have been entitled to receive all of the assets if the liquidation provisions of the charter were applicable. The objecting preferred stockholder claimed that the proposed liquidation

was an involuntary dissolution within the meaning of the charter, and this claim was the issue before the Court.

In rejecting the claim, this Court reasoned as follows: The applicability of the charter provision in this context is a federal question (323 U. S. at p. 636). The charter was adopted six years before the Act, and the simplification under the Act "having as an incident to it the dissolution of one company in a holding company system, was not an anticipated 'liquidation' within the meaning of Power's charter provision" (Ibid. at p. 637). The reason "lies in the fact that Congress did not intend that its exercise of power to simplify should mature rights . . . which otherwise would only arise by voluntary action of stockholders or, involuntarily, through action of creditors" (Ibid. at p. 638). This language makes it plain that the "involuntary" preference in the charter refers to action taken as a result of insolvency, and "voluntary" preference to action taken by the stockholders. It is precisely the latter type of action which is involved in the instant case.

In the *Central-Illinois* case, the position was reversed. Engineers Public Service Company was seeking to dissolve to meet the requirements of the Act. It was willing to pay to the preferred stockholders the "involuntary" liquidation preference, but not the higher "voluntary" preference. The Commission, relying on the *Otis* case, awarded the latter amount as the equitable equivalent of the investment. This Court, in affirming that decision, stated that "the principal effect of the *Otis* decision" was that "the *involuntary* charter liquidation preference does not determine of itself the amounts shareholders are to receive . . ." (338 U. S. at p. 129). If the charter provisions were applicable, "of course it would follow that those provisions are the measure of equitable equivalence" (Ibid. at p. 131). However, "the equitable equivalent is not invariably the charter liquida-

tion preference, *as it is in the case of liquidations or reorganizations brought about through the action of creditors or stockholders.*" (Italics added.) (Ibid. at pp. 130-131).

In the *Otis* case, this Court stated that Congress would wish "to preserve values to investors, not to destroy them", and again: "Enforcement of an overriding public policy should not have its effect visited on one class with a corresponding windfall to another class of security holders." (323 U. S. at pp. 636-637). The same thought is expressed in *Central-Illinois,* in reference to "the fact that Congress, in its efforts to achieve a particular economic goal, wished to avoid shifting investment values from one class of securities to another . . ." (338 U. S. at p. 134).

That such would have been the results if those cases had been decided otherwise is clear. In the *Otis* case, the then value of the enterprise was less than the liquidating preference of the preferred stock. However, the earnings were in excess of the dividend requirements and, if the enterprise could be continued, dividends could eventually have been paid on the common stock. The preferred stockholders could not have required the dissolution of the enterprise and, apart from the requirements of dissolution imposed by the Act, the common stockholders had a valuable economic interest supported by their contract. To have held that the Act required payment of the involuntary liquidation preference would have resulted in transferring to the preferred stockholders the economic interest of the common stockholders, solely by reason of the Act. This Court's view that Congress did not intend such a result is readily understandable. Similarly, in the *Central-Illinois* case, the common stockholders could not have forced the preferred stockholders out of the enterprise by paying to them the involuntary liquidation preference of their securities. To eliminate the preferred stock, it would have been necessary

for the common stockholders either to call the preferred or to dissolve through corporate action, and in either event the preferred would have been entitled under the charter to the sum ultimately awarded them. In that case, to have upheld the claims of the *common* stockholders would have shifted to them an economic interest which the preferred stock had under the charter.

No such situation is presented where, as in the case of Federal, the common stockholders in good faith vote to dissolve and offer to pay the full amount specified in the charter in such event. Preferred stockholders in such a case cannot claim more than that amount since that is what they have bargained for. In such circumstances, there is no investment value shifted because there is nothing to shift.

The Commission had itself taken the same view in *In re El Paso Electric Company*, Holding Company Act Release No. 5499 (1944), which it refused to follow and the Court of Appeals rejected (R. 220 and 265). Although that case was decided a few weeks before this Court's decision of the *Otis* case, the investment value doctrine had been thoroughly established by the Commission's decisions, and had been upheld by the courts, including the District and Circuit Courts in the *Otis* case itself (see Appendix to the *Central-Illinois* opinion, 338 U. S. 155).

In the *El Paso* case it was proposed that El Paso be liquidated and dissolved in accordance with Delaware law and that its preferred stockholders be paid $100 per share and accrued and unpaid dividends as provided in the charter in the event of voluntary liquidation. The Commission found that the holding company in question had disposed of all but one of its operating subsidiaries in compliance with divestment orders of the Commission, and that the retirement of its preferred stock and its own liquidation

had become necessary under the standards of Section 11(b) of the Act by virtue of such divestment orders. The Commission held, nevertheless, that the payment to the preferred stockholders of the *voluntary* charter liquidation preference (which was less than the call price) would satisfy the "fair and equitable" standard of Section 11(e) even though the fair investment value might have been greater, stating:

> "Solely on an earnings and dividend basis, the Series A preferred stock may well be worth more than $100 per share plus accrued dividends. However, appraisal of the stock on that basis is unrealistic in view of the charter limitation provision and the non-functional character of the company. Engineers, as the dominant stockholder, must of course refrain from using its controlling voting power to effect a transaction unfairly benefiting itself at the expense of public investors, and we may not permit the operation of Section 11(b) of the Act to destroy legitimate investment values. But wholly apart from Section 11(b), elimination of El Paso's corporate entity is an economically desirable step, and the power to take that step does not arise from Section 11(b) but is found in the contract fixing the rights, preferences and limitations of the security holders affected.
>
> "In the circumstances of this case we are satisfied that action taken by Engineers to liquidate El Paso will constitute a *bona fide* exercise of its voting rights, existing wholly apart from Section 11, and that the proposed liquidation properly brings into operation the rights and limitations prescribed by the certificate of incorporation for just such a contingency. The investment interests of the preferred and common stock are being terminated pursuant to existing contract provisions, and are being compensated as provided in the contract."

(H. C. A. Release No. 5499, at pp. 7-8).

The Commission's reasons for refusing to apply the doctrine of the *El Paso* case are set forth in its Supplemental Findings and Opinion (R. 220) in the instant case as follows:

> "Federal has argued that our decision in *El Paso Electric Company,* S. E. C. (1944), Holding Company Act Release No. 5499, is controlling in the instant case. In that case we approved as fair a Section 11(e) plan in which compensation for the surrender of the preferred stock interest was limited to the amount of the charter liquidation preference after finding that '. . . wholly apart from Section 11(b), elimination of El Paso's corporate entity is an economically desirable step . . . .' An examination of the opinion in that case shows that, though we referred to the impact of Section 11(b) generally, we placed great weight upon the non-functional status of the company as it existed at the time of its proposed liquidation. As we have shown in the preceding analysis of the Federal system and the divestments which it made, it is our view that in determining whether or not Federal would have liquidated absent the integration and simplification requirements of the Act, the inquiry to be made is whether the reduction in the size and any other changes in the system which preceded the liquidation, as well as the final step in the liquidation process, were the result of such requirements. This approach thus differs from that followed in the *El Paso* case, and accordingly we cannot consider the latter case as determinative of the issues now before us."

The foregoing passage would seem to indicate that, where the Act constitutes a contributory motive to the determination of the common stockholders to terminate the enterprise in accordance with the provisions of the charter, the contractual basis of payment evidenced by the charter provisions will be disregarded. It is believed that such treat-

ment is grossly unfair to the common stockholders. In any event, it presents a new and significant application of the "fair and equitable" standard, and should be reviewed by this Court.

2. Under the Commission's divestment orders[5] issued in the course of Section 11(b)(1) integration proceedings, Federal was permitted to retain four utility subsidiaries operating in New Mexico and one operating in Colorado. The last such order was issued on March 30, 1944.[6] In December, 1945, Federal voluntarily disposed of the Colorado subsidiary and it voluntarily merged the four New Mexico subsidiaries in September, 1946, thereby reducing itself to the status of a holding company with but one operating subsidiary. Immediately thereafter it filed the original application with the Commission seeking permission to dissolve and liquidate by vote of its stockholders in accordance with New York law.

Neither the Commission nor the court below have questioned the fact that Federal's liquidation could not have been required under the Act if Federal had elected to continue as a holding company for the five New Mexico and Colorado subsidiaries. Under different economic conditions it might well have continued as a holding company, as probably would have been the case, for example, if the World War II excess profits tax law had continued in effect, in which event substantial tax savings would have resulted by reason of Federal's favorable tax base credit which shielded a large portion of the earnings of its retain-

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[5] *Cities Service Power & Light Company*, H. C. A. Release No. 4489 (1943); *Federal Light & Traction Company*, H. C. A. Release No. 4960 (1944).

[6] *Federal Light & Traction Company*, H. C. A. Release No. 4960 (1944).

able subsidiaries from the excess profits tax (R. 106). Accordingly, it is pertinent to inquire why the exercise by Federal's common stockholders of their option to terminate the enterprise should require a theoretical appraisal of the "investment value" of the preferred stock, or how the amount arrived at through such an appraisal can exceed the amount which the common stockholders agreed to pay and the preferred stockholders agreed to accept.

As has been pointed out in the preceding discussion of the *El Paso* case, the holding company in that case had no alternative but to liquidate after having complied with the Commission's divestment orders, whereas here it was solely as the result of actions which could not have been required or compelled by the Act that Federal was liquidated. Accordingly, even if the *Otis* and *Central-Illinois* cases may be deemed to render a voluntary charter liquidation preference inoperative where, as in the *El Paso* case, liquidation was compelled by the Act, it still remains for this Court to determine whether the same principle should apply to a liquidation which could not have been compelled by the Act.

II.

1. The Commission's decision rests upon its appraisal of "the fair investment value" of the preferred stock "as if the company were a going concern" (R. 207). In this connection, the Commission stated:

> ". . . In doing so we give appropriate weight to all factors relevant to investment value, including charter provisions as to liquidation which are taken into account in all cases but are not deemed controlling except when it is clear that liquidation would have taken place for reasons unrelated to the integration and simplification requirements of the Act."

(R. 207).

The Commission accorded no weight whatsoever to the probability of liquidation apart from the requirements of the Act. The record shows that, prior to the issuance of the Commission's first divestment order in 1943, Federal had disposed of properties representing more than 50% of its total investment, and the Commission's findings concede that "strong business reasons existed for" those divestments "aside from the necessity of complying with the integration requirements of the Act" (R. 210). Extensive evidence was adduced by Federal to show that, apart from the Act, there existed valid business reasons for disposing of virtually all of the relatively few properties that actually were ordered to be divested (R. 15, 89-95, 120-121, 195) and to show that the liquidation of Federal would have been economically desirable and feasible if the Act had not been in existence (R. 106-7). The Commission concluded, nevertheless, that "absent the impact" of the divestment orders "liquidation for purely business reasons would not have occurred, and that therefore the liquidation preference ceases to be a dispositive factor in determining the investment value of the preferred stock" (R. 219).

Obviously, a conclusion that liquidation would have occurred "for purely business reasons" would have made the charter liquidation preference *solely* dispositive. However, it is clearly open to question whether a finding that "liquidation for purely business reasons would not have occurred" is justified on the face of the Commission's own findings. Certainly the "likelihood of liquidation", which is what the Commission set out to appraise, is a matter of degree. If there was any substantial evidence to show that business reasons existed for liquidation apart from the requirements of the Act, and it is respectfully submitted that there was, it seems incumbent upon the Commission to evaluate the likelihood of liquidation in the form of a discount from the call price.

The Commission's determination is not in accord with its holding in the case of *In re American Light & Traction Company*, Holding Company Act Release No. 6603 (1946). Although no claim was made in that case that liquidation might have occurred apart from the Act, the Commission evaluated the mere possibility of liquidation at approximately 50% of the difference between the charter liquidation price and the higher fair investment value determined on a basis which gave no weight to the possibility of liquidation. In so doing, the Commission took into account the fact that in the case of a holding company, as distinguished from an operating company, "there would undoubtedly be some possibility of voluntary liquidation, a possibility which would always be present and which prudent investors could not ignore." (H. C. A. Release No. 6603, at p. 28).

In the instant case, the Commission found that Federal had not demonstrated that it would have liquidated if the Act had not been in existence (R. 215). That finding forms the basis for the Commission's conclusion that the preferred stockholders might be entitled to more than the voluntary charter liquidation preference. It is submitted, however, that, to hold that the preferred stockholders were entitled to the full redemption price, the Commission was required to find that the prospect of liquidation apart from the impact of the Act was negligible. This apparently was recognized by the Commission's staff, which, as recited in the Commission's Supplemental Findings and Opinion (R. 208), urged that such a finding be made. *But that finding was not made.* The Commission's determination of the "investment value" is unsupported by a necessary basic finding and, therefore, is not arrived at in accordance with legal standards. *United States* v. *Carolina Freight Carriers Corp.*, 315 U. S. 475, 488-89; See, *Opp Cotton Mills*

Inc. v. *Administrator,* 312 U. S. 126, 144; and see *United States* v. *Baltimore & Ohio R. R. Co.,* 293 U. S. 454, 464; cf., *Universal Camera Corp.* v. *N. L. R. B.,* ..... U. S. ....., Case No. 40, October Term, 1950, February 26, 1951. Also, the review of the facts by the Court of Appeals was not directed to this issue.

2. In the *Central-Illinois* case, this Court said: "Valuation on the basis of a going-concern necessarily has primary relationship to value as of the time the shareholders' surrender becomes effective, not as of some earlier, remote period, or one long afterward." (338 U. S. at p. 139). This Court also said that the agency is not supposed to "... value the stock as if the Act had never affected the holding company system of which the particular company dealt with in the plan is a part." (Ibid.). In the instant case, the situation at the time of the proposed dissolution was as follows: The assets of Federal consisted substantially of a large amount of cash, representing the proceeds from the sales of former subsidiaries, plus all of the common stock of Public Service, its sole remaining operating utility subsidiary; dividends from Public Service plus such income as might be derived from the investment of the cash was the sole foreseeable source of income to Federal; Federal's actual income at that time was barely sufficient to meet the dividend requirements on the preferred stock; the prospect of profitable employment of the cash on hand was severely curtailed by the limitations contained in the Act on investments in public utility securities.

The Commission apparently recognized that on the basis of the existing factual situation a finding that the fair investment value of the preferred stock was greater than the charter liquidation preference, $100, could not be justified. Nevertheless, the Commission awarded the call price,

$110, using two alternative hypotheses. As its first hypothesis, the Commission assumed (R. 223) that Federal still owned many of the properties already disposed of, in which case the Commission considered the income would be sufficient to support the finding that the fair value of the preferred stock was $110. As its alternative hypothesis, the Commission assumed (R. 237) that the excess cash would be reinvested in public utility securities of the same general quality as those previously held by Federal, in which case the Commission likewise considered that the earnings would be sufficient to justify its result. By its first hypothesis, the Commission restored to the enterprise certain of the properties which were not retainable—thereby attributing to the preferred stockholders income which neither the enterprise nor the common stockholders could be then in a position to receive. The second hypothesis amounted essentially to the same thing, for the investments which the Commission assumed could be made were forbidden by the very Act which the Commission was purportedly applying.

In support of its position, the Commission has argued that this Court's decision in the *Central-Illinois* case did not prescribe an exclusive method of valuation. It is submitted, nevertheless, that the principle of that case was violated, and that the result is contrary to fairness and equity.

Conclusion.

It is respectfully submitted that this petition for a writ of certiorari be granted.

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